

Message Text

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ACTION ARA-10

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TAGS: ECON, CI

SUBJECT: GOC OFFICIALS ADMIT SLOW PROGRESS IN ANTI-INFLATION PROGRAM

1. SUMMARY. GOC AUTHORITIES NOW ACKNOWLEDGE THAT MONTHLY INFLATION RATE NOT LIKELY TO GO BELOW PRESENT 8 PERCENT UNTIL LATE 1976. PART OF FAILURE TO REACH GOAL OF 5 PERCENT MAY BE EFFORTS BY BUSINESSMEN TO RECOUP LOSSES EARLIER IN YEAR, TO STRUCTURAL PROBLEMS WITHIN MONETARY SYSTEM, TO BOP PROBLEMS, AND POSSIBLY TO GOC RELAXATION OF ANTI-INFLATION MEASURES IN VIEW OF HARDSHIPS WHICH PRESENT AUSTERITY POLICIES ARE IMPOSING.
END SUMMARY.

2. CENTRAL BANK'S VICE PRESIDENT ALVARO BARDON AT A SEMINAR RECENTLY HELD IN SANTIAGO, NOTED THAT MONTHLY INFLATION RATES SHOULD CONTINUE AT THE PRESENT LEVEL (AROUND 8 PERCENT) FOR SEVERAL MONTHS AHEAD. THE ANTI-INFLATION PROGRAM WOULD CONTINUE, HE ADDED, BUT AT A SLOW PACE. HE INDICATED THAT INFLATION PRESSURES ARE ORIGINATED MAINLY BY THE EXCESSIVE LIQUIDITY OF SAVING INSTRUMENTS OF THE SAVINGS AND LOAN SYSTEM, THE DEFICITS OF STATE ENTERPRISES AND THE MALFUNCTIONS OF
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THE NEWLY DEVELOPED CAPITAL MARKET.

3. BARDON AND FINMIN CAUAS SEPARATELY HAVE COMMENTED TO ECON COUNSELOR THAT THE "REAL" CAUSE OF THE GOC'S INABILITY TO REDUCE THE MONTHLY RATE LIES IN CHILE'S OBLIGATION TO PAY ON ITS DEBTS AND COMPENSATION OBLIGATIONS. THIS LINE ALSO TAKEN BY EL MERCURIO. BECAUSE THE GOC LACKS DOLLARS DERIVED FROM ITS OWN COPPER EARNINGS TO PAY ON THESE DOLLAR OBLIGATIONS, THE GOC IS INSTEAD COMPELLED TO BUY WITH PESOS DOLLARS EARNED BY CHILEAN EXPORTERS. THESE PESOS PASS INTO THE ECONOMY AND HELP TO INCREASE THE MONEY SUPPLY. ECON COUNSELOR ASKED CAUAS WHETHER EXPORTERS WOULD NOT SWAP DOLLARS FOR PESOS ANYWAY, WHATEVER THE LEVEL OF COPPER EARNINGS. CAUAS' REPLY WAS THAT ABSENT THESE DOLLAR OBLIGATIONS (AND ASSUMING SOMEWHAT MORE NORMAL COPPER PRICES), CHILE WOULD NOW HAVE A SURPLUS OF COLLARS. CHILE WOULD THEREFORE EXPORT SOME OF ITS OWN INFLATION BY REVALUING ITS PESO UPWARD, INCREASING IMPORTS AND REDUCING EXPORTS. CHILE CANNOT, HOWEVER, TAKE THESE ANTI-INFLATIONARY STEPS BECAUSE IT IS GIVING PRIORITY TO HONORING ITS INTERNATIONAL OBLIGATIONS. (WE WOULD CONCEDE TO CAUAS AND BARDON THAT THIS FACTOR IS NOT UNIMPORTANT. IT IS, HOWEVER, FAR FROM THE WHOLE STORY. WE DETECT IN THE EXPLANATIOO PROFFERED BY CHILE'S ECONOMIC TEAM A HINT OF A DESIRE TO SHIFT THE BLAME FOR THE MEDIOCRE PERFORMANCE OF ITS ANTI-INFLATION PROGRAM TO EXTERNAL FORCES, BESIDES REMINDING THE AMERICANS OF THE DOMESTIC PRICE THAT CHILE IS PAYING FOR ITS INTERNATIONAL FINANCIAL RECTITUDE.)

4. TO THE TEAM'S CREDIT, THE GOC'S ANTI-INFLATION PROGRAM GOAL OF LIMITING MONTHLY INCREASES TO FIVE PERCENT FOR THE LAST QUARTER OF 1975 WAS NOT UNREALISTIC AT THE TIME IT WAS SET. SANTIAGO'S STORES IN THE PAST USUALLY TRADED LOWER PRICES FOR LARGER VOLUMES OF SALES AT THE END OF THE YEAR. THIS WAS REFLECTED IN LOWER CONSUMER PRICE INDEX (CPI) RATES DURING THESE PERIODS. HOWEVER, BUSINESSMEN HAVE ACTED DIFFERENTLY THIS YEAR, SINCE THE LEVEL OF SALES AND PRODUCTION EXPERIENCED FOR THE YEAR AS A WHOLE HAS BEEN THE LOWEST OF THIS DECADE. IN EFFECT, THEY ARE NOW TRYING TO RECOVER PART OF THE YEAR'S LOSS. NOVEMBER'S CPI HAS EXCEEDED LAST YEAR'S BY 1.5 POINTS AND DECEMBER'S WILL PROBABLY SHOW AN EVEN LARGER DIFFERENTIAL.

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5. EQUALLY POSSIBLE, THE FAILURE TO GET DOWN TO FIVE PERCENT LEVEL MAY REFLECT THE GOC'S OWN DECISION NOT TO ENFORCE ITS ANTI-INFLATION PROGRAM QUITE SO VIGOROUSLY. SOCIAL COSTS SUCH AS THE UNEMPLOYMENT RATE AROUND 16-17 PERCENT, A PROJECTED FALL IN GNP OF 12 PERCENT AND A HEAVY LOSS OF PURCHASING POWER FOR THE AVERAGE WAGE EARNER, ALL EXCEEDING WHAT WAS INITIALLY THOUGHT LIKELY, ARE SUBJECT TO CRITICISM

WHICH IS INCREASINGLY HARD TO IGNORE.

6. MOREOVER, MORE LABOR INTENSIVE PROGRAMS HAVE BEEN INCLUDED IN 1976'S FISCAL BUDGET, AND THE PRESENT SYSTEM OF QUARTERLY READJUSTMENTS OF WAGES AND SALARIES BASED ON CPI WILL CONTINUE THROUGHOUT NEXT YEAR. (LATTER WAS CONSIDERED UNNECESSARY EARLY IN 1975, DUE TO THE LOW RATES OF PRICE INCREASES THAT WERE EXPECTED FOR 1976 AT THAT TIME.) ALL THESE SHOULD ADD TO INFLATIONARY PRESSURES IN 1976.

7. IN SHORT, THE GOC'S INABILITY TO MEET ITS ANTI-INFLATIONARY GOALS SEEMS TO BE THE RESULT OF A COMBINATION OF FACTORS. IT IS DIFFICULT TO TELL WHAT WEIGHT TO GIVE ANY ONE OF THEM AT THIS TIME.
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